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Evaluating Nebraska Banks

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Introduction

At no time since the Great Depression has the banking industry experienced the problems it faces today. The number of banks failing nationwide in 1988 reached a post-Depression high of 200. The number of bank closings in each of the last seven years has set new post-Depression highs. The number of bank failures in each of the last 15 years is shown in Table 1.

Table 1
Number of Bank Failures Per Year

Year	Bank Failures
1974	4
1975	13
1976	16
1977	6
1978	7
1979	10
1980	10
1981	10
1982	42
1983	48
1984	79
1985	120
1986	138
1987	184
1988	200

The banking industry posted a record profit of $25.3 billion in 1988 with the highest return on assets (.84 percent) since 1973. Ironically, the industry recorded a record number of failures during the same year. How can this be? Many banks, primarily larger ones, are doing well, while many banks, primarily smaller to medium size ones, are experiencing difficulties.

The purpose of this article is twofold: to present reasons for the recent proliferation of bank failures and to present a way to identify problem banks in Nebraska.

Bank Failures—Why So Many?

Numerous reasons are given for the recent increase in bank failures. For example, the deregulation of the banking industry in the early 1980s greatly enhanced competition within the industry. To maintain profit margins in the face of increased competition, many bankers sacrificed quality and made loans that ordinarily would not have been made. Loans often were made outside the bankers' areas of expertise, and numerous loan portfolios were allowed to become heavily concentrated. In attempts to remain competitive, many bankers used poor judgment and overexposed their banks to economic downturns.

Another factor contributing to bank failures is the prevailing restriction against branch banking. Branching limitations inhibit diversification of risk and may promote concentrations of credit. If more branch banking had been allowed in recent years, perhaps many bank failures could have been avoided—healthy

State Economic Scoreboard

Change from same month one year ago.
See Review and Outlook on page 8 for more details.

	State	Metro+	Nonmetro
Motor Vehicle Sales (December) Constant $	-16.6%	-14.0%	-18.6%
Nonmotor Vehicle Sales (December) Constant $	0.1%	1.1%	-1.0%
Building Activity (December) Constant $	15.3%	8.6%	24.4%
Employment (February)	4.3%	3.6%	5.1%
Unemployment Rate* (February)	2.8%	2.5%	3.2%

+Omaha and Lincoln. *Unemployment is this month's rate, not a percent change from year ago.

branches would have absorbed the losses of unhealthy branches.

The reason most often given for the increased number of bank failures is the depressed economies of the oil and agricultural states in the last several years. For example, Nebraska suffered 26 bank failures from 1985-1988.

Fortunately, the economic climate in the region recently has begun to improve. With the improving economic environment, one might assume that bank failures are a thing of the past.

A 1988 study by the Office of the Comptroller of the Currency (OCC), however, indicates that the economic climate is not the primary cause of bank failure. The OCC study of 162 national bank failures since 1979 concluded that oversight and management deficiencies were the primary factors that caused bank failures. Poor policies and planning, especially concerning loans, were major problems in 89 percent of the banks that failed.

Based on this extensive OCC study, it appears that increased competition, restrictions against branch banking, and poor economic conditions are not the direct causes of bank failure. Poor management is the primary cause. These other factors combine to bring the management deficiencies to light sooner. Thus, as long as poor managerial practices exist, banks will continue to fail.

Depositors Beware!

As Knapp notes in a May 1985 *Journal of Accountancy* article, the proliferation of bank failures presents a possible problem to corporate depositors. Because deposits are guaranteed by the FDIC up to $100,000 only, large corporate depositors face a real potential for loss if total deposits in a failed bank exceed this limit. The potential for loss also exists for noncorporate depositors. Although the average individual customer's deposits fall below the $100,000 guarantee, it is not uncommon for affluent customers to have multiple accounts (e.g., checking, passbook savings, certificates of deposit, etc.) exceeding the $100,000 limit.

To avoid the potential for loss, depositors should maintain large accounts in banks run by sound management, which best can be determined by looking at the financial health of a bank.

The Z Index for Possible Bank Failures

To construct the Z index, data from 25 Nebraska banks that failed during the period 1985-1988 were combined with comparable data from nonfailed Nebraska banks for the same period. (Twenty-six banks failed during this period, but data were not available for one bank.)

Each failed bank was matched with a nonfailed Nebraska bank of approximately equal asset size. A match based on size made it possible to isolate differences in operating performance, rather than size.

The differences between the failed and nonfailed banks were determined by examining 30 financial ratios for the year-end prior to the year of failure. Ratios were obtained from call report information provided by Sheshunoff and Company.

The ratios provide measures of loan quality and loan concentration, capital adequacy, earnings ability and operating efficiency, liquidity, and bank growth. The ratios (all ratios are percentages—not decimals) that differed most significantly between the failed and nonfailed banks were:

* *Return on Assets (ROA)*—Income (or loss) before extraordinary items to average total assets. Measures the recent earnings ability of bank management in terms of a return on assets invested.
* *Primary Capital to Assets (PRIMCAP)*—Primary capital, consisting mainly of equity capital plus loan loss reserves, to average total assets. Measures the past earnings capability of management and indicates the cushion available to absorb future losses.
* *Overhead to Assets (OVERHEAD)*—Total of salaries and benefits, occupancy expense, and other operating expense to average earning assets. Measures management's efficiency with respect to overhead. A low percentage is favorable, while a high percentage is unfavorable.
* *Nonperforming Loans to Gross Loans (NONPERF)*—Total year-end loans and leases at least 90 days past due plus loans placed in a nonaccrual status to gross year-end loans and leases. Measures quality of bank's loan portfolio.
* *Loans to Assets (LOANS)*—Gross year-end loans to total year-end assets. Measures bank management's willingness to accept risks. A relatively high percentage indicates that management has accepted greater risks by investing a larger portion of assets in loans.

Table 2 shows the average amounts for each ratio for the failed and nonfailed Nebraska banks included in the sample. The relationships between the failed and nonfailed bank ratios are as expected and are indicative of the unhealthy status of the failed banks prior to their closure. These means are useful, as they provide benchmarks against which all Nebraska banks can be compared. Even more useful than the means is the model developed for identifying problem banks.

Table 2
Mean Ratios for
Failed and Nonfailed Banks

Ratio	Failed Banks	Nonfailed Banks
ROA	-1.95%	1.03%
PRIMCAP	7.83%	13.74%
OVERHEAD	4.30%	3.28%
NONPERF	10.21%	1.80%
LOANS	63.64%	43.94%

Multiple discriminant analysis (MDA) was used to develop the Z index to differentiate between failed and nonfailed banks. MDA involves deriving a linear combination of the independent variables (the five ratios) that best discriminates between the two groups. The resulting discriminant function or Z index is shown below:

$$Z = 1.25656 + .06351\,(ROA) + .01983\,(PRIMCAP) - .07280\,(OVERHEAD) - .00960\,(NONPERF) - .01130\,(LOANS)$$

The Z index for a particular bank is compared to a cutting Z score to determine the bank's predicted classification. The cutting Z score is .5. A bank with a calculated Z index less than .5 is classified as having characteristics of a nonfailed bank.

To evaluate the accuracy of the Z index method, it was tested on the 50 Nebraska banks included in the study. Although not perfect, the method was reasonably accurate; 48 (96 percent) of the banks were classified correctly. One failed bank was misclassified as a nonfailed bank, and one

nonfailed bank was misclassified as a failed bank.

Using the Z index is simple and can be demonstrated easily with an example. Assume three banks (A, B, and C) are being analyzed by a potential banking customer or investor. Further, assume that the three banks have the operating statistics for their most recent year-end as shown in Table 3. Such information is generally available on a timely basis from the FDIC or private firms (e.g., Sheshunoff and Company). Plugging these amounts into the Z index function yields the following Z index scores:

A = 1.25656 + .06351(-.37) + .01983(10.33) - .07280(3.40) - .00960(5.71) - .01130(40.62) = .677

B = 1.25656 + .06351(-1.94) + .01983(6.73) - .07280(2.52) - .00960(7.89) - .01130(56.73) = .367

C = 1.25656 + .06351(1.12) + .01983(10.29) - .07280(1.89) - .00960(4.64) - .01130(46.67) = .822

Notice that bank B's Z index is below the cutting Z score of .5, while the Z indexes for banks A and C are above .5. This indicates that bank B possesses the characteristics of banks that have failed in the past, whereas banks A and C possess the characteristics of nonfailed banks. This does not necessarily mean that bank B will fail while A and C will not. It means that bank B's operating statistics are similar to those of banks that failed in the past, while the statistics for banks A and C are similar to those of banks that did not fail in the past.

Perhaps even more useful than classifying banks using the cutting Z score is ranking the banks. The Z indexes produced by the Z index method provide an ordinal ranking of the financial health of the banks. The higher the Z index, the greater the financial strength. For instance, the three banks used in this example would be ranked from strongest to weakest as follows:

	Z index
Bank C	.822
Bank A	.677
Bank B	.367

Any or all Nebraska banks can be ranked in this manner. One final note with respect to the Z index method is a word of caution. The method is not a panacea. Because numerous factors cannot be captured in a mathematical model, the method is not intended to replace a user's judgment. It simply is intended to provide an additional piece of information as input into the user's decision making process.

Conclusion

Bank failures in recent years have increased at phenomenal rates. The primary reason for the failures seems to be poor management. The problem of managerial deficiencies is compounded by the competitive banking environment, restrictions against branch banking, and poor economic conditions. These failures have caught the attention of the regulators and the public alike.

This article offers a method for detecting future possible bank failures The method could prove most useful when supplemented with knowledge on subjective factors such as the quality of bank management and/or the economic prospects of the community in which a bank operates.

Table 3
Ratios for Example Banks

Ratio	Bank A	Bank B	Bank C
ROA	-.37%	-1.94%	1.12%
PRIMCAP	10.33%	6.73%	10.29%
OVERHEAD	3.40%	2.52%	1.89%
NONPERF	5.71%	7.89%	4.64%
LOANS	40.62%	56.73%	46.67%
Z INDEX	.677	.367	.822

Libraries in Nebraska

According to the Nebraska Library Commission and the *Nebraska Blue Book, 1988-1989*, Nebraska's first library was established at the Fort Atkinson military post in 1820. The federal Kansas-Nebraska Act of May 20, 1854 provided a territorial library in Nebraska that later became the state law library.

The state's first public library was established in Omaha in 1871. In 1877, the state legislature passed a law providing state support of public libraries. A state library commission with responsibility for promoting, developing, and coordinating library services in Nebraska was established by the legislature in 1901.

Today Nebraska has approximately 50 academic libraries, 286 public libraries, 646 school media centers, 22 institutional libraries, 134 special libraries, and 84 county law libraries.

Love Library, located on the University of Nebraska-Lincoln campus, is the largest library in the state with a collection of approximately 1.7 million volumes. Other large libraries include the collection at the Nebraska Library Commission, the Nebraska State Library, the Lincoln City Libraries; the Omaha Public Library; and academic libraries at Creighton University and the University of Nebraska at Omaha.

These libraries participate in regional multitype service systems that provide regional support and coordination. Nebraska libraries are linked through an electronic telecommunications network to NEON, the data base of Nebraska library holdings, and to other state and national data bases.

For further information about libraries in Nebraska contact:

Nebraska Library Commission
1420 "P" Street
Lincoln, NE 68508
(402) 471-2045

Merlin W. Erickson

Global Competition: Midwest Perspective

Robert Milligan, President and CEO, MI Industries, Lincoln, Nebraska

In this paper, I will review Nebraska's role in international markets and the importance of export markets to Nebraska, the Midwest, and the U.S. I also will give an overview of economic issues that may come to the forefront in the next few years.

Let us set the stage with a background on what may happen in the 1990s. The New *York Times* and *Fortune* have christened this decade as the *era of possibilities*. Why has this decade been so named? In my opinion, we see the greatest economic opportunities since the end of World War II. We also see some of the greatest competition that we have ever known.

In Europe, we foresee the opportunity for a unified Western Europe starting in 1992. What are the implications of that unification? It means 325 million persons under a more unified system—the most unified European system the world has known in modern economic times. Europe will replace the U.S. as the world's largest, richest market

Add to Western Europe the potential that is developing for 140 million Eastern Europeans. Now add another 40 million free associate state Europeans. And finally, add the potential for 250 million Soviet customers. That brings a total of nearly 800 million customers in a targeted area. Over half those economies, or 400 million consumers, are calling for a total restructuring of their economies. The potentials are enormous.

When I started to discuss global opportunities, I may have assumed something I shouldn't assume—namely that all of us in this state, particularly with our great concern and understanding for agribusiness, look at the world as a place in which we should compete economically. In my opinion, we have only two choices: to close our borders (Nebraska or U.S.), selling and producing strictly on an internal basis, or to try to obtain a level playing field in a global arena and participate (compete) as effectively as we can in that arena. I favor the second choice of global competition

The stage is being set by a number of our political leaders, including Secretary Yeutter in the Uruguay Round. Clayton Yeutter is trying to develop a level playing field for all export competition. What does the opportunity to compete worldwide mean for Midwest or Nebraska agriculture?

Let's ask our neighbors, the Kansas wheat farmers. They would resist closing our borders because over 60 percent of their wheat crop currently is exported. Roy Frederick dramatically underscored the importance of the livestock industry to Nebraska's gross agricultural income; 60 percent to 65 percent of Nebraska's gross agricultural income comes from the livestock industry. Last year in the U.S., beef exports increased over 60 percent from the year before. For the first time, America exported more than a billion pounds of beef

Unlike the years immediately after World War II when we saw great opportunities and relatively little competition, we see our trading partners poised for strong competition. Japan is a strong competitor . . . Look at the Japanese automobile and microchip industries. Look at Britain in foods, service, and publishing; West Germany in pharmaceuticals and chemicals; Australia and Argentina in beef; France, Canada, Argentina, and Brazil in grains: These are strong competitors ready to participate in the world market.

I would like to touch briefly upon four key concepts that I believe point to a positive economic trend for the world in the 1990s. I believe that these factors support the position that the 1990s will be the decade of possibilities.

1. Democracy continues to advance globally, bringing economic change for the world. South Korea, the Philippines, Argentina, Poland, and Chile all are evolving dramatically toward a more democratic form of government. These political changes, in turn, imply economic changes in these countries.

India has ended 40 years of Gandhi rule peacefully. We also are witnessing the emergence of a more democratic form of government and changing economies in Hungary, East Germany, and Czechoslovakia. The Congress of the People's Deputies has called for free, nonmonopolistic (communist) elections in the Soviet Union. President Gorbachev's response only was to question the timing of the idea, not its merit.

Certainly there will be reversals in this trend toward a more democratic world. We have seen that in the Philippines and in Poland, where real income has dropped 20 percent. Most reversals there were due to unmet or unrealistic economic expectations, lack of capital, lack of convertible currencies, or hyperinflation. Even with the dramatic changes we have seen in leadership, stifling bureaucracies remain.

Only 70 of the 170 societies in the world today quality as free, even using the broadest definition of the term. But I don't think there's any question that the Marxism/Leninism model is under siege.

2. There will be a lessening of tension because of the decreasing possibility of large scale military conflict. This shift means that economic performance rather than military power will count more in the future. No wonder Russia and its leadership are running fast to stay ahead of the crowd. We have seen President Gorbachev labeled the man of the decade, more influential than President Reagan. I submit that it makes no difference who's leading the Politburo. The changes in the Soviet Union were necessary because of economic changes in the world.

There always will be regional and historic tensions, such as that between Korea and Japan (there are no Japanese cars in Korea), even though we don't have large scale tensions.

Proposed reductions in military budgets over the next several years may alter our own economic development. Think of the possibilities of a $100 billion reduction in our U.S. military budget over the next several budget cycles.

3. We will continue to see a global community that will increase its technical and technological advantages. It will be smarter; we'll continue to see the world shrinking because of a vast communications explosion.

Since the mid-1960s, the percentage of high school age population enrolled in

secondary education almost has doubled worldwide. College enrollment also has doubled worldwide in the last 20 years. This presents a great opportunity for telecommunications.

An official from Corning is excited about the possibility of rebuilding the telephone systems in the Soviet Union with optical fibers because there are no copper wires to remove. Even in Russia and Eastern Europe, we must be aware of the advance of science and technological ability. They have more than one-third of the world's Ph.D.-level engineers and scientists. We see advanced technology coming from these societies—soft contact lenses, surgical staples, and great advances in metallurgy, to name a few.

4. Economic interdependence of the world community will continue. Since 1950, world trade has grown twice as fast as world Gross Domestic Product. Think about what that means. Certainly, it's going to cause some uneasiness. Think of the editorials about Japanese investment in the U.S. That makes us uncomfortable.

What about Nebraska in the global competition arena? Can we compete? In the aggregate, I would say we are well prepared; we have an educated workforce that should be able to adapt. Also, our base industries in food/fiber are moving ahead. We are seeing increased focus, awareness, and participation by many Nebraska industries in sales throughout the world.

We constantly must tend the store, however. I think the U.S. now has a better focus on that than they have had in the past. We must be willing to change our businesses, to be flexible. This will mean:

1. Thinking globally.
2. Thinking new alliances (joint ventures, etc.).
3. Thinking of new ways of doing business (barter, etc.).

An Exchange Student View of Japan

Jack Hardy, Bureau of Business Research, Undergraduate Research Associate

In an era of an increasing significant international market, it is important that any business education include a study of international issues. Any study of international business should place considerable emphasis on Japanese business practices.

For the student interested in Japan, the University of Nebraska-Lincoln College of Business Administration sponsors a study abroad program at Senshu University in Tokyo.

Last semester I participated in this program and earned credits studying Japanese language, business, and civilization, while experiencing firsthand what it is like to live in a Japanese community.

At the University of Nebraska-Lincoln, I have studied basic issues related to Japanese business practices in practically every one of my business courses. The material was introductory, however, and often failed to address my particular interests in the social and cultural forces that shape Japanese commercial practices.

How are Japanese management practices, which are different from traditional American practices, applied so successfully in Japanese culture? Why does the average Japanese businessperson feel such a strong sense of organizational loyalty toward his or her company? Why are many aspects of Japanese business puzzling to Americans?

With these interests in mind, I traveled to Japan to study with 12 other students from the University of Nebraska and two students from Susquehanna University in Pennsylvania. For 12 weeks we studied Japanese language for three hours every morning and listened to lectures on Japanese business and civilization in the afternoon. Our language instruction was introductory because most of us had little, if any, experience with Japanese.

This lack was not a great hindrance for us, however; most of our instructors spoke English. Most Japanese students we met spoke some English, having studied English for six or seven years. Almost all Japanese were anxious to practice their English with us.

The business and culture lectures were presented by different faculty members of Senshu University and professional persons from the community. We heard lectures on topics such as "The Evolution of Japanese Management," "Traditional Japanese Human Relations," "The History of U.S.-Japanese Trade Conflict," and many others. Each day brought new lectures on topics that our hosts thought would be of particular interest to us.

My most memorable experiences were those outside the classroom. We visited modern institutions such as the Tokyo Stock Exchange and the Diet Building. The Diet Building houses the legislative body of Japanese government. We went on field trips to businesses and manufacturing plants such as Nissan Motor Corporation, Matsushita Research Institute, and Kirin Beer. We also went sightseeing at different historical sites, traditional temples, and shrines. During all our trips and experiences outside the classroom, we were accompanied by faculty members or Japanese students. Japanese students were as eager to try to understand us and our culture as they were to help us understand Japanese culture.

My study of Japan was valuable because I was able to integrate what I was learning about Japanese history, culture, and philosophical tradition with what I was learning about Japanese business practices.

For example, I learned that Japanese management practices such as promotion according to seniority, lifetime employment, and bottom-up decision making can be viewed as vestiges of ancient Confucian notions of filial piety, loyalty, and collective harmony.

I also discovered that as a result of their heritage as a communal society, the Japanese tend to identify strongly with the various groups with which they are associated. The tendency to feel a strong sense of corporate loyalty also can be viewed as a remnant of traditional Japanese society.

Given Japan's historic growth remote from western civilization, it is hardly surprising that American and Japanese culture and their respective business practices differ. If we fail to recognize and

educate ourselves about the differences that do exist, we will continue to limit our ability to cooperate with, compete with, or influence Japan and the Japanese people.

The Japanese are focused on international issues. As a result, years of English language study are a compulsory component of every student's education.

From the moment I arrived, it was apparent that the Japanese students I met were going to take advantage of my presence. They were anxious to practice their English and learn whatever I could teach them about America.

It is on this point that we may take an important lesson from Japan. It would be, without a doubt, to our advantage to treat our international students at the University of Nebraska as valuable educational resources.

My experience in Japan made it clear to me that America's future success in international commerce depends, to a large extent, on how willing Americans are to understand other cultures.

There are opportunities for generating cross-cultural understanding abroad, as well as with the large population of international students at our university. I encourage all students and faculty at the University of Nebraska to take advantage of these opportunities.

Other international study opportunities available to College of Business Administration students include these summer programs:

* Oxford Program—Dean Gary Schwendiman, leader
* Orient Study Tour—Professors Harish Gupta and Roger F. Riefler, leaders
* Moscow Visit—Dr. Robin Anderson, leader
* Budapest School of Economics Program—Associate Dean J. Clay Singleton, leader
* The annual Pan Pacific Conference will be held May 31-June 2 in Seoul, Korea. Professor Sang M. Lee, program chairman, expects 300 participants.

Jack Hardy is a senior in economics. He is one of three undergraduate research associates with the Bureau of Business Research this spring semester. Jack is working on a project to calculate and analyze nonmetro nonfarm per capita personal income in Nebraska.

Population Growth Continues for Most Urban Areas 1980-1988

Two hundred and thirty-three of the nation's 283 metropolitan statistical areas (MSAs) gained population during the 1980-1988 period, according to recent estimates by the Bureau of the Census of the U.S. Department of Commerce. Twenty-three of the 50 MSAs that lost population are located in Michigan, New York, Ohio, Pennsylvania, and West Virginia. Four are located in Iowa.

Nebraska's two MSAs of Omaha and Lincoln gained population during the 1980-1988 period. According to Bureau of Census estimates, however, the Omaha

Table 1
Estimates of Population and Net Migration Change for the MSAs of Nebraska and Neighboring States 1980-1988

State	Population Change		Net Migration Change	
	Number	Percent	Number	Percent
Colorado				
Pueblo	1,700	1.3	-4,800	-3.8
Denver-Boulder	239,500	14.8	79,400	4.9
Greeley	12,800	10.3	1,000	0.8
Colorado Springs	84,500	27.3	43,400	14.0
Fort Collins-Loveland	32,800	22.0	18,700	12.5
Iowa				
Sioux City, IA-NE	-1,800	-1.5	-8,700	-7.4
Iowa City	5,000	6.1	-2,100	-2.6
Waterloo-Cedar Falls	-15,000	-9.2	-23,800	-14.6
Dubuque	-2,800	-3.0	-7,400	-7.6
Des Moines	24,200	6.6	-300	-0.1
Davenport-Rock Island-Moline, IA-IL	-20,500	-5.3	-41,800	-10.9
Cedar Rapids	1,700	1.0	-8,600	-5.1
Kansas				
Topeka	9,900	6.4	1,200	0.8
Wichita	40,700	9.2	600	0.1
Lawrence	8,800	13.1	3,900	5.8
Missouri				
Joplin	8,400	6.6	4,500	3.5
Kansas City, MO-KS	141,900	9.9	47,300	3.3
St. Joseph	-2,500	-2.8	-4,800	-5.5
Columbia	5,400	5.4	-2,500	-2.5
St. Louis, MO-IL	89,700	3.8	-42,500	-1.8
Springfield	26,600	12.8	16,500	8.0
South Dakota				
Sioux Falls	16,100	14.7	7,100	6.4
Rapid City	11,700	16.6	2,400	3.4
Nebraska				
Lincoln	18,700	9.7	4,500	2.3
Omaha, NE-IA	36,500	6.2	-11,100	-1.9

MSA experienced a net migration loss of 11,100. Net migration is defined as the difference between gross inmigration and gross outmigration. Gains in natural growth (births minus deaths) more than offset the migration loss.

Table 1 provides statistics on population and net migration change for the MSAs of Nebraska and neighboring states for 1980-1988.

For reporting purposes, the Sioux City, IA-NE MSA is listed under Iowa. Similarly, the Omaha, NE-IA MSA is listed under Nebraska.

MSAs are defined by the Office of Management and Budget (OMB) in terms of whole counties outside New England and individual towns and cities in New England.

The general concept of a MSA is that of a population nucleus of at least 50,000, generally consisting of a city and its immediate suburbs, together with adjacent communities having a high degree of economic and social integration with that nucleus.

An area qualifies for recognition as an MSA in one of two ways: If there is a city of at least 50,000 population or a Census Bureau-defined urbanized area of at least 50,000 with a total metropolitan population of at least 100,000 (75,000 in New England).

In addition to the county containing the main city, an MSA also includes additional counties having strong economic and social ties to the central county, determined chiefly by the extent of the urbanized areas as defined by the Census Bureau and census data on commuting to work.

MSAs with major population and(or) net migration changes for the 1980-1988 period are indicated in Table 2.

By 1988, the nation's MSA population had reached 189.4 million, amounting to 77.1 percent of the U.S. total of 245.8 million. Another 56.4 million persons lived in nonmetropolitan territory outside the 283 MSAs.

Since 1980, the population of metropolitan America, as currently defined, has increased 16.8 million (9.7 percent), well above the national average increase of 8.5 percent. Nonmetropolitan American increased only 2.4 million (4.5 percent), less than half the metropolitan rate of growth.

Most metropolitan population growth continues to occur in the Sunbelt and Far West. The metropolitan areas in the North grew only 2.2 million (2.6 percent) from 1980 to 1988, while those in the South and West grew 14.6 million (16.6 percent).

From 1980 to 1988, metropolitan areas grew faster than nonmetropolitan areas in 35 states, while the nonmetropolitan areas had the edge in 14 states. (New Jersey and the District of Columbia are entirely metropolitan.) The states with more rapid nonmetropolitan growth are Massachusetts, Rhode Island, Connecticut, Delaware, Maryland, Florida, California, Alaska, Hawaii, West Virginia, Ohio, Michigan, Wisconsin, and Wyoming.

F. Charles Lamphear

Table 2

MSAs that Gained over 1/2 Million in Population

MSA	Population Growth
Los Angeles-Anaheim-Riverside	2,272,000
Dallas-Ft. Worth	835,500
San Francisco-Oakland-San Jose	673,900
Atlanta	598,400
New York-Northern New Jersey-Long Island	580,700
Houston-Galveston-Brazoria	541,500
Phoenix	520,400
San Diego	508,600

MSAs that Gained over 250,000 by Net Migration

MSA	Net Migration Gain
Miami-Fort Lauderdale	269,700
San Francisco-Oakland-San Jose	309,100
San Diego	332,000
Phoenix	369,000
Tampa-St. Petersburg-Clearwater	382,000
Atlanta	414,000
Dallas-Fort Worth	496,600
Los Angeles-Anaheim-Riverside	1,142,700

MSAs that Lost over 50,000 in Population

MSA	Population Loss
Pittsburgh-Beaver Valley	-139,200
Detroit-Ann Arbor	-132,500
Buffalo-Niagara Falls	-67,200
Cleveland-Akron-Lorain	-65,100

MSAs that Lost over 50,000 by Net Migration

MSA	Net Migration Loss
Detroit-Ann Arbor	-364,300
Chicago-Gary-Lake County	-290,000
Cleveland-Akron-Lorain	-180,200
Pittsburgh-Beaver Valley	-168,100
Buffalo-Niagara Falls	-99,400
New York-Northern New Jersey-Long Island	-92,800
Milwaukee-Racine	-92,700
New Orleans	-50,400

MSAs Where Deaths Exceeded Births

Bradenton, FL
Daytona Beach, FL
Sarasota, FL
Scranton-Wilkes-Barre, PA
Tampa-St. Petersburg-Clearwater (ranked 10th in actual population growth)

Review and Outlook

John S. Austin, Bureau of Business Research, Research Associate

National Outlook

The second revision of the fourth quarter 1989 Gross National Product (GNP) statistics is now available. These figures will remain official until the July revision. In general, this set of numbers shows a stronger economy than did the preliminary numbers. This set of figures improves our view of the fourth quarter and will help us speculate on the first quarter of this year.

The fourth quarter increase was 11.2 billion 1982 dollars at annual rates. Unfortunately, most of that increase, $9.9 billion or some 86.1 percent, can be accounted for by a change in net exports. Net exports are simply exports minus imports. The net export figure itself is a fairly small component of GNP and, furthermore, tends to contain a great many data errors. Put another way, without the strong positive net export figure, GNP would have grown only about .1 percent, instead of the revised 1.1 percent in the latest figures.

Net exports has been a source of strength in the last few years. Early indications, however, are that first quarter net exports may be weak. A surge in oil imports of 44 percent in January implies a weak net export figure for the first quarter. That, in turn, implies that we should be looking elsewhere for strength.

Table I
Real GNP Fourth Quarter 1989
Change from Third Quarter

	Change $ billion (1982)	Percent of Total Change
Consumption	3.6	31.3
Investment	-7.1	-61.7
Government	5.1	44.3
Net Exports	9.9	86.1
Total	11.2	100.0

Note: There is a rounding error of 0.3 billion in the total.

Consumers increased their purchases 3.6 billion 1982 dollars. Virtually all of the increase was due to increases in consumer services. Durable spending decreased $16.1 billion. That decrease alone was bigger than the total gain in real GNP in the quarter. The decrease in durables was due to an automobile sales collapse.

Looking at first quarter figures, January was a good month for autos, but February data show a reversal. Unless there is a major dealer incentive program instituted early in March, first quarter auto sales likely will remain weak, pointing to a weak consumer durable number. Relatively high prices of energy and food in January in turn imply a weak nondurable consumption figure. All these suggest that the first quarter will show a weak consumption sector. Confusing this picture somewhat, the retail sales reports for January and February show a substantial advance over fourth quarter numbers. At best, consumption offers a mixed picture.

In the government sector, we see a seesaw pattern from quarter to quarter. The fourth quarter showed a decrease in federal spending offset by an increase in state and local spending. The total showed an increase of 5.1 billion 1982 dollars, 44.3 percent of the total increase in GNP. In the first quarter, we expect more cuts in federal defense expenditures, implying a weak federal sector. State and local spending will continue to grow and is likely to offset the decrease in federal spending. On the whole, I expect a small plus for total government spending in the first quarter of 1990.

Things start to get interesting in the investment block. In total, the investment

Table II
Employment in Nebraska

	Revised January 1990	Preliminary February 1990	February % Change vs. Year Ago
Place of Work			
Nonfarm	706,857	712,339	3.3
Manufacturing	95,789	95,673	2.1
Durables	46,715	46,700	1.3
Nondurables	49,074	48,973	2.8
Mining	1,232	1,284	-1.8
Construction	22,395	22,249	8.4
TCU*	46,328	46,583	4.1
Trade	184,279	182,986	2.7
Wholesale	53,978	53,924	5.5
Retail	130,301	129,062	1.6
FIRE**	48,557	48,560	2.0
Services	167,028	170,006	3.5
Government	141,249	144,998	3.9
Place of Residence			
Civilian Labor Force	823,693	826,557	3.72
Unemployment Rate	3.1%	2.8%	

*Transportation, Communication, and Utilities
**Finance, Insurance, and Real Estate

Source: Nebraska Department of Labor

Table III
Price Indices

	February 1990	% Change vs. Year Ago	YTD % Change vs. Year Ago
Consumer Price Index - U* (1982-84 = 100)			
All Items	128.0	5.3	5.2
Commodities	120.6	5.5	5.4
Services	136.0	5.1	5.1
Producer Price Index (1982 = 100)			
Finished Goods	117.4	5.1	5.5
Intermediate Materials	112.5	1.4	2.0
Crude Materials	106.9	5.8	5.7
Ag Prices Received (1977 = 100)			
Nebraska	161	0.6	0.6
Crops	125	-11.3	-10.6
Livestock	184	6.4	5.8
United States	153	3.4	3.4
Crops	135	-2.2	-2.5
Livestock	171	8.2	8.5

U* = All urban consumers
Source: U.S. Bureau of Labor Statistics

sector decreased 7.1 billion 1982 dollars in the fourth quarter. Virtually all the decrease was in producers' durable equipment expenditures. That group had been a source of strength in 1987 and 1988. In 1989, the increases in producers' durable equipment investment slowed.

In the first quarter 1990, there is some hope that producers' durable equipment expenditures will return to the plus column. In addition, we have seen some recovery in the housing area. The latter increases could be shut off if long-term interest rates continue to climb. Housing starts have been the one ray of hope in our previous educated guesses for the 1990 outlook. Recent mortgage rate increases, however, have diminished hopes for a rapid recovery in that sector. Diminished hopes in the housing sector imply that the chances of a more rapid overall recovery are lessened.

Both consumer and producer prices jumped dramatically in January as a result of cold weather on the east coast. Cold weather created a surge in demand for fuel oil and damaged fruit and vegetable crops in Florida. In February, we saw a mixed result. Decreasing energy prices allowed the Producer Price Index to remain even with January levels; however, consumer prices rose 0.5 percent in February. The increase in consumer prices was a result of a mixture of events. There was an 18.7 percent drop in fuel oil prices, but a sharp 3.3 percent jump in clothing prices. Food prices grew 0.5 percent in February. The clothing price index was unique, being related to an early introduction of spring clothes. The increase in apparel is not expected to be repeated in the March figures. Thus, there is some hope of further easing in the Consumer Price Index for March. Nevertheless, inflation has to be monitored closely. It is rapid inflation and an improper reaction by monetary authorities that often have been associated with economic downturns.

There are two predominant schools of thought about what will happen to interest rates in the next few months. One school posits that our weak domestic economy will allow the Federal Reserve to stimulate the economy further by lowering interest rates. There is little doubt that the Fed can control short-term interest rates, especially the Federal Funds rate. The Fed

Table IV
City Business Indicators
December 1989 Percent Change from Year Ago

The State and Its Trading Centers	Employment (1)	Building Activity (2)
NEBRASKA	0.1	17.1
Alliance	-0.9	-62.4
Beatrice	-0.1	84.0
Bellevue	-0.3	42.3
Blair	-0.3	-34.8
Broken Bow	0.4	-94.7
Chadron	-0.7	-3.9
Columbus	0.7	75.3
Fairbury	0.8	7.3
Falls City	-0.4	75.1
Fremont	-0.3	37.6
Grand Island	-0.6	-20.9
Hastings	0.0	62.7
Holdrege	0.1	695.1
Kearney	0.9	94.6
Lexington	1.3	111.3
Lincoln	1.1	25.3
McCook	1.0	186.1
Nebraska City	-0.1	175.7
Norfolk	0.1	49.4
North Platte	-0.5	10.9
Ogallala	-0.7	-6.7
Omaha	-0.3	-1.1
Scottsbluff/Gering	-0.5	-7.4
Seward	0.7	35.7
Sidney	1.0	-60.0
South Sioux City	-1.7	-51.3
York	-0.5	16.9

(1)As a proxy for city employment, total employment (labor force basis) for the county in which a city is located is used

(2)Building activity is the value of building permits issued as a spread over an appropriate time period of construction. The U.S. Department of Commerce Composite Cost Index is used to adjust construction activity for price changes

Sources: Nebraska Department of Labor and reports from private and public agencies

Figure I
City Business Index
December 1989 Percent Change from Year Ago

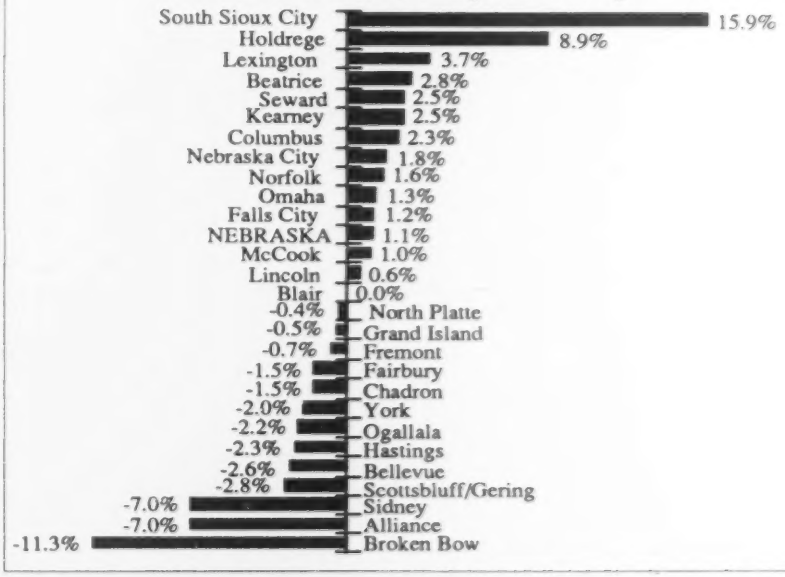
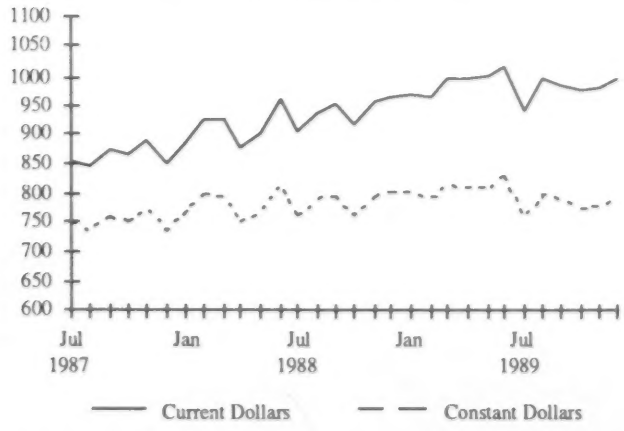


Table V
Net Taxable Retail Sales of Nebraska Regions and Cities

Region Number and City (1)	City Sales (2) December 1989 (000s)	City Sales (2) % Change vs. Year Ago	Region Sales (2) December 1989 (000s)	Region Sales (2) % Change vs. Year Ago	Region Sales (2) YTD % Change vs. Year Ago
NEBRASKA	$1,125,019	4.7	$1,219,349	3.1	6.0
1 Omaha	406,039	7.7	477,712	5.5	7.3
Bellevue	18,255	-5.6	*	*	*
Blair	5,723	9.4	*	*	*
2 Lincoln	144,137	1.9	158,900	1.8	3.4
3 South Sioux City	6,900	51.3	8,592	38.0	15.8
4 Nebraska City	4,482	-2.9	19,245	0.8	2.6
6 Fremont	18,973	-0.8	32,960	-2.1	4.2
West Point	3,489	11.6	*	*	*
7 Falls City	2,760	1.0	10,116	-4.8	-0.8
8 Seward	5,613	5.7	16,838	-2.6	2.0
9 York	8,398	-1.8	17,707	-4.3	3.7
10 Columbus	19,299	2.5	31,514	-0.2	4.4
11 Norfolk	25,156	3.2	40,796	-0.9	4.7
Wayne	3,278	6.0	*	*	*
12 Grand Island	45,078	6.2	59,660	5.7	7.7
13 Hastings	19,439	-6.7	30,010	-2.9	5.2
14 Beatrice	10,493	3.8	21,302	-2.1	1.3
Fairbury	3,619	-1.0	*	*	*
15 Kearney	24,310	1.6	32,275	0.3	7.1
16 Lexington	7,787	3.0	18,279	-3.5	4.9
17 Holdrege	5,091	1.5	8,521	-4.9	4.9
18 North Platte	20,028	2.5	24,148	2.0	6.2
19 Ogallala	5,903	0.5	11,433	-5.5	8.7
20 McCook	9,467	-6.4	12,798	-7.8	2.2
21 Sidney	4,594	-2.9	8,614	-3.2	-1.0
Kimball	1,849	0.3	*	*	*
22 Scottsbluff/Gering	23,287	-1.1	30,410	-0.3	6.3
23 Alliance	6,322	-0.3	15,806	-6.9	2.1
Chadron	3,420	1.7	*	*	*
24 O'Neill	5,396	3.6	16,265	-0.7	9.6
Valentine	3,073	3.4	*	*	*
25 Hartington	1,778	11.6	9,330	-1.7	1.2
26 Broken Bow	4,288	10.5	13,315	-2.1	3.9

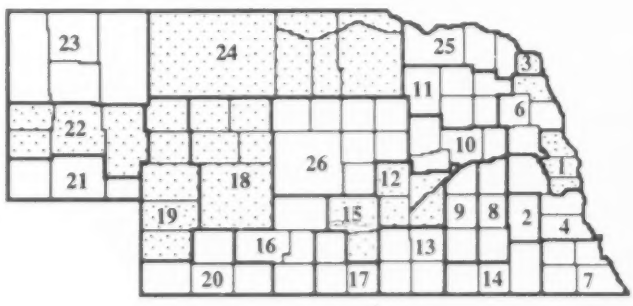
(1) See region map
(2) Sales on which sales taxes are collected by retailers located in the state. Region totals include motor vehicle sales
* Within an already designated region
Compiled from data provided by the Nebraska Department of Revenue

Figure II
Nebraska Net Taxable Retail Sales
(Seasonally Adjusted, $ Millions)



(1) The Consumer Price Index (1982-84 = 100) is used to deflate current dollars into constant dollars

Figure III
Region Sales Pattern
YTD as Percent Change from Year Ago



Shaded areas are those with sales gains above the state average. See Table V for corresponding regions and cities

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has nailed the Federal Funds rate at 8.25 percent for several months now.

The other major school of thought argues that long-term rates are set in an international market. Both the Japanese and the Germans are experiencing rising long-term interest rates. The U.S. must follow these rates if it is to remain competitive in the international arena. If not, we will see a capital outflow from the U.S. to other countries.

The review of these two approaches reminds one of the old forecasters' axiom that "if it doesn't go up, it'll go down, if it doesn't stay the same." My best guess is that risks are on the up side, especially in the long-term markets. International pressures will impact our domestic long-term markets. Further, there is some cause for concern on inflation, as nonfood and nonenergy prices are showing some increases.

Nebraska Outlook

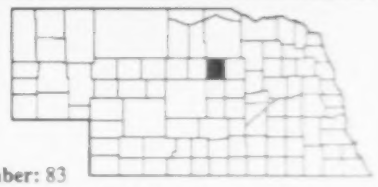
Retail sales are available for all of 1989. For the year as a whole, there was an advance of 6.0 percent (see Table V upper right corner). With inflation rates on consumer goods at 4.5 percent, the nominal growth that Nebraskans have experienced translates to a 1.5 percent real growth in retail sales. Sales were fairly flat from March on. Nebraska's December season was somewhat listless.

Year-end labor force data show virtually no change from year-end 1988 (Table IV). In contrast, February job gains were 3.3 percent ahead of year ago (Table II), continuing a trend of job gains outpacing increases in the labor force. The two fastest growing job areas were wholesale trade and construction.

Early year construction data are available from F. W. Dodge. So far the state has continued last year's stellar performance. Through February, year-to-date total contracts have increased 28.6 percent. Total building square footage has increased 50.4 percent. New dwelling contracts have increased 54.4 percent. All of these increases must be taken with a grain of salt. The early months of the years are influenced heavily by weather changes. In our case, both January and February were relatively good building months. Should the March figures reinforce the January-February numbers, then Nebraska construction may be started on an extremely good year.

County of the Month

Garfield



Burwell--County Seat

License plate prefix number: 83
Size of county: 570 square miles, ranks 64th in the state
Population: 2,100 (estimated) in 1988, a change of -9.3 percent from 1980
Median age: 38.7 years in Garfield County, 29.7 years in Nebraska in 1980
Per capita personal income: $11,558 in 1987, ranks 88th in the state
Net taxable retail sales ($000): $12,038 in 1988, a change of +20.4 percent from 1987; $11,981 during 1989, a change of -0.5 percent from the same period one year ago
Number of business and service establishments: 82 in 1987; 62.2 percent had less than five employees
Unemployment rate: 4.6 percent in Garfield County, 3.6 percent in Nebraska for 1988
Nonfarm employment (1988):

	State	Garfield County
Wage & salary workers	688,146	632
	(percent of total)	
Manufacturing	13.8%	8.7%
Construction and Mining	3.8	4.9
TCU	6.5	3.2
Retail Trade	18.5	22.5
Wholesale Trade	7.3	9.6
FIRE	7.0	3.8
Services	23.0	22.3
Government	20.1	25.0
Total	100.0%	100.0%

Agriculture:

Number of farms: 248 in 1987, 268 in 1982
Average farm size: 1,314 acres in 1987
Market value of farm products sold: $18.8 million in 1987 ($75,818 average per farm)

Sources: U.S. Bureau of the Census, U.S. Bureau of Economic Analysis, Nebraska Department of Labor, Nebraska Department of Revenue

Merlin W. Erickson

Business in Nebraska

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